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November 16, 2004

**BY E-MAIL**

Keith Rake  
Deputy Assistant Commissioner  
Bureau of the Public Debt  
Department of the Treasury  
P.O. Box 396  
Parkersburg, WV 26101-0396

Re: Proposed Amendments to SLGS Program Docket Number BPD-02-04  
69 *Federal Register* 58756, September 30, 2004

Dear Mr. Rake:

The American Bankers Association (“ABA”) is responding to the proposal issued by the Department of the Treasury (“Treasury”) that would amend the current rules governing the sale and redemption of State and Local Government Series (“SLGS”) securities. The ABA brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership—which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks—makes ABA the largest banking trade association in the country.

Many of our members serve as escrow agents or indenture trustees (collectively “escrow agents”) of defeasance trusts and are concerned that, in its current form, the proposal would impose on them significant obligations that they are unable to perform. Accordingly, while ABA supports the goals intended to be achieved in the proposal, as discussed more fully below, we seek changes that would address the inherent limitations that exist when our members serve in these fiduciary capacities.

## **Background**

SLGS are Treasury obligations purchased by state and local government entities directly from Treasury to assist such issuers to comply with yield restriction and rebate requirements applicable to tax-exempt securities under the Internal Revenue Code. SLGS securities are not available for purchase or trading on the open market.

Treasury has expressed concerns that when issuers engage in certain practices with respect to redemptions before maturity and subscription cancellations, they are, in effect, using the SLGS program as a cost-free option contrary to the purposes of the program. In addition, Treasury believes these practices create volatility in the agency's cash balances, make cash balance forecasting more difficult, and increase its borrowing costs. To eliminate these practices, Treasury has proposed, among other things, to:

- Limit any changes in the aggregate principal amount of submitted subscriptions to no more than ten percent;
- Prohibit any change in the selected issue date; and
- Require certain certifications from "subscribers."

An escrow agent holds the funds representing proceeds of refunding bond issues pursuant to written agreements with the issuer that govern the actions of the escrow agent in this fiduciary capacity. Among other things, these governing documents establish both the manner in which the funds being held are to be invested, and when and how they are to be paid out. All investment actions are limited by these documents and, as appropriate by the issuer or its counsel and/or financial advisors. *Importantly, the escrow agent has no discretion in these matters.*

One of the duties escrow agents are required to perform under the governing documents is subscribing for SLGS. As a result, escrow agents become "subscribers" for purposes of the SLGS regulations. Such subscriptions occur as directed either (1) prior to or concurrent with the refunding bond issue, or (2) subsequent to the closing of the refunding bonds. In either case, the actions must be taken according to a fixed schedule in the escrow agreement. Again, the escrow agent has no discretion to deviate from these terms or directions. To do so independently could be deemed to be a violation of the escrow agent's duties under the governing documents.

ABA is concerned that the proposal may impose on escrow agents, duties that conflict with the limitations on their authority in the typical escrow governing documents and which, in turn, could lead to the imposition of penalties on them. ABA believes that neither of these results were intended by Treasury.

## **Discussion**

### ***1. Prohibition on Changes in Issue Date or Amount***

Escrow agents are instructed under the governing documents to reinvest gross proceeds held in escrow accounts in SLGS (usually zero percent). In connection with such reinvestments, clerical errors occur from time to time with respect to, for example, the amount invested, the interest rate, the maturity date, or the settlement date. Similarly, from time to time, the settlement date for a new issue of refunding bonds maybe delayed as a result of circumstances beyond the control of the issuer, as in the case of a natural disaster or litigation.

ABA strongly believes there *must* be a reasonable and efficient process for correcting such errors without penalty to the issuer or the escrow agent. Under the current rules, subscribers are permitted to amend Time Deposit and Demand Deposit subscriptions by extending the delivery date of the SLGS up to seven days after the delivery date originally specified in the subscription. However, under the proposal, once a SLGS subscription is submitted, there could be *no* change in the issue date; nor could the aggregate principal amount be changed by more than ten percent.

ABA believes that the current time frame in which to take corrective actions has served this particular purpose well, and we urge Treasury to retain the existing provision. Nonetheless, should that not serve Treasury's broader purposes, we strongly believe that there must be some process through which to make these types of corrections.

### ***2. New Subscriber Certifications***

Under the proposal, subscribers would be required to provide a number of new certifications including:

- If the issuer is purchasing with proceeds of a sale or redemption, that the yield on the SLGS not exceed the yield at which the securities was sold; and
- The bonds have been authorized and provide a description of the bonds to be issued and various other certifications.

In addition to these certifications, the proposal includes two requirements over which escrow agents have no control:

- That the purchase of SLGS is from gross proceeds only; and
- The maturity is no longer than is reasonably necessary to accomplish the governmental purpose of the issue.

***Limited authority of escrow agents.*** Under the proposal, SLGS subscribers that are escrow agents acting pursuant to the governing documents or at the direction of the issuer or its authorized agents would be required to certify matters of which they may have no knowledge. Similarly, the proposal includes requirements about which escrow agents have no knowledge or control. Therefore, ABA believes the proposal should be amended to (1) require issuers to provide to their escrow agents the required certifications and/or statements of compliance with Treasury's requirements, and (2) provide that escrow agents may rely on such certifications/statements on their face without further action by the escrow agents.

Alternatively, ABA requests that the SLGS subscription forms be revised to define the "subscriber" as the party actually directing that the subscription be placed—the issuer or its agent (*e.g.*, an underwriter).

In addition, we request that the actual subscriptions (including any cancellation and redemption activity associated therewith) filed with the Bureau of the Public Debt show as the subscriber the same party so defined on the subscription forms—the party that *in fact* directed the escrow agent to take the action. These changes would permit Treasury to most directly and efficiently identify the responsible parties.

Finally, it is unclear whether the certifications are required on each scheduled rollover of SLGS or just on the initial subscription. In many instances, all of the required investments are set forth in the governing documents and there is little or no further contact with the issuer. ABA requests that Treasury clarify (1) that the initial authorization contained in the governing documents also authorizes the escrow agent to make all scheduled rollover and other SLGS investments throughout the life of the escrow; and (2) the initial certifications/statements extend to all rollovers under the same subscription.

In addition, ABA believes that scheduled rollovers made pursuant to escrow agreements in existence prior to the effective date of a final rule should remain subject to the current rules.

***Prior authorization of issuance.*** Under the proposal, the subscriber would be required to certify that the issuer has already authorized the *issuance* of the state or local bonds. However, ABA's members advise that in many states in which they do business, issuers typically authorize the *sale* of bonds, but not the *issuance* of the bonds until several days after the bonds have actually been sold. Because SLGS subscriptions need to be made concurrently with the sale and prior to the authorization of the issuance of the bonds, as the SLGS subscriber, escrow agents have no authority to make such certifications under the typical escrow.

Accordingly, ABA requests that Treasury revise the proposal to state that by issuing a direction to the escrow agent to subscribe for the purchase of SLGS, the issuer shall be deemed to have represented and warranted such authorization. In the alternative, we urge Treasury to amend the proposal to require the issuer to provide to the escrow agent a certification or opinion of bond counsel that such authorization has, in fact, occurred.

### **Conclusion**

In conclusion, ABA supports the goals of the proposal. However, we request certain changes to ensure that escrow agents are able to properly comply with those goals while adhering to the limitations on their authority under escrow agreements. ABA would appreciate the opportunity to discuss these issues further with you, and we look forward to working with you.

Sincerely,

A handwritten signature in cursive script, reading "Cristeena G. Naser".

Cristeena G. Naser